City of GLEN EIRA

Reference:
Enquiries:
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Glen Eira City Council

80 MCGs of parklands
enough footpaths to reach Sydney
enough drains to reach Mildura
enough roads to reach South Australia
;00m of town planning projects
2,000 food safety inspections
4,000 off-street car spaces
23,000 tonnes of recycling
32,000 tonnes of waste
one million library loans
care for 4,500 elderly
services for 8,000 children
6,200 immunisations
67 school crossings
46,000 street trees
8,500 street lights
45 sports grounds
47 playgrounds
and much more

Mr Chris Pattas
General Manager Network Investment and Pricing
Australian Energy Regulator
GPO Box 520
MELBOURNE VIC 3001

Dear Mr Pattas,

Re: Electricity Distribution Price Review - Submission

Thank you for the opportunity to comment on your issues paper. Please note that the attachments to this letter are to be treated as confidential.

I am writing to respond in regards to the question related to public lighting and specifically whether a negotiated outcome could work. The fact that Council has not commented on other issues associated with pricing or demand management should not be interpreted as meaning that Council has no comments, rather, Council has not had the available resources to consider these issues in detail.

This response covers operational issues for Council rather than policy issues. The response has been prepared by officers responsible for delivery of the relevant functions of council. They have been mindful of the objectives of Council's community plan and the need to comply with the following Principles of Sound Financial Management as contained in section 136 of the Local Government Act: prudently manage financial risks relating to debt, assets and liabilities; and consider the financial effects of Council decisions on future generations.

You asked *"We welcome comments on whether a negotiated outcome could work? What elements can/or should be negotiated? What specifically do customers want changed in the regime now"*

Council's preference is that OMR remain regulated for the next period primarily because negotiation is already in theory possible, and therefore removing regulated prices does not add a solution for councils, rather, it removes a safeguard.

Also, Council doesn't have confidence that it will be readily able to negotiate good outcomes for Council; and, even if it could in theory, it may not be able to do so without high investment of time and resources which are not currently available. Council is not clear if or how a negotiated outcome would interact with its requirements to tender works under section 186 of the Local Government Act of Victoria and this would need to be understood to understand if there are any implications.

More detail is provided below about why officers have formed this view and their experience in attempting to negotiate in the past.

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If AER intends to proceed with approval of a negotiated outcome (which Glen Eira City Council does not support) AER should ensure there are safeguards including:

- Required response timeframes
- Requirements for transparency when distribution companies quote, including requirement for a suitable level of detail in order to understand the components and contributing factors to quotes for works.
- An easy to use dispute/supervision process that can be accessed in a timely manner
- Triggers that provide for updates to O and M prices if the market changes (for example if supply prices change)
- To reduce transaction costs, pricing, once negotiated should be standardised in some way and not require individual negotiation by each council.

If AER does not intend to approve a negotiated outcome, Council would seek:

- Triggers that allow repricing for OM&R for example if supply prices change.
- Requirements for transparency when distribution companies quote, including requirement for a suitable level of detail in order to understand the components and contributing factors to quotes for works.

In both cases, AER should also clarify how any change may affect the following practices:

- Application and calculation of WDV and avoided costs
- Project administration fee pricing

<u>Detailed explanation:</u>

Council understands that the reason AER is considering separating replacement (R) from O and M is to reduce the split incentive currently experienced where distribution businesses do not consider lifetime costs when replacing lights.

- The Public Lighting Code requires distribution businesses to minimise *"costs to public lighting customers"* (clause 2.1(c)), which should be adequate to address the split incentive if interpreted over the lifecycle of the asset. Unfortunately, this seems to have historically been interpreted to mean lowest capital cost, which Council doesn't regard as a reasonable interpretation.

- Council supports the aim of removing the split incentive, but is not convinced that negotiating is the best method for solving the problem.

- Generally, Council is also supportive of changes that would increase competition in the provision of O,M and R services (note that Council is also of the view that the specific details of how this is done are important). However, Council's understanding of the current changes proposed is that they would not prevent a distribution company preventing others working on their assets and retaining an effective monopoly if they choose.

- O and M estimates are key inputs into the business case for councils when considering Replacement projects (which is often done on an asset lifetime basis using NPV or other financial tools). To do this, councils must be able to obtain estimates of OM&R costs in advance before commitment to a replacement project. The Victorian Public Lighting Code (clause 3.2.2) implies that commitment from councils may be required before an OMR price would be provided by a distribution company for a new type of light – without a regulated price and considering clause 3.2.2 of the public lighting code, councils may be effectively prevented from receiving information needed to make decisions about replacement.

Distribution companies are often more expensive than other providers and we don't have high confidence that quotes for OM&R will be best value for Council and the community:

- At Glen Eira City Council, we deal with both UE and CitiPower. UE allows Council to engage approved contractors to do work on their network to bulk change lights, but CitiPower requires Council to order works through them. Council understands that the changes proposed will not require CitiPower to change this approach (nor prevent UE using the same approach in future) which does not address the issue of an effective monopoly being place.

- In 2012 and 2013, when Council engaged contractors to change its 5000+ MV80 streetlights on the UE network to more efficient lights the project costs (including all costs paid by Council for installation, supply and project management) were around 35 per cent lower cost than works quoted and provided by CitiPower – this illustrates the potential value of competitive processes to procure services.

- Council also delayed the above project to wait for approval of a second T5 product, which reduced the supply costs for the project (Council thinks this is likely due to the price competition a second supplier created, but does not have evidence).

- Quotes for minor works for replacement of the same lights have been priced very differently suggesting that some level of monopoly pricing to a captive market may be in use. For example, quotes received for contestable minor works in late 2014 varied between the two distribution companies from under $700 to over $3000 (see confidential attachment A).

Council's attempts to negotiate have been unsuccessful

- Council attempted to negotiate with CitiPower unsuccessfully on a number of grounds (see confidential attachment B).

- The unequal power in this negotiation meant that it was in practice not possible for Council to achieve a better price despite also knowing that CitiPower's price was high compared to the market.

Successful negotiation would require time and resources that are not available

- Council would need adequate skilled resources available to successfully negotiate – it would require new staff or contractors to manage and run this process. To illustrate the challenge, for example, Council has not been able to review in detail the distribution business proposals as part of the Electricity Distribution Price Review in order to respond, nor been able to attend many of the consultation sessions.

- Negotiating as a group would be important for councils to be effective – this would require decision making structures to be set up and funded at regional level which do not currently exist.

Distribution companies haven't developed a reasonable range of replacement products for use on their network within a reasonable timeframe.

- Despite a wide range of more efficient lighting being available in the market, very few are approved and available for use on distribution networks in a way that would minimise costs for customers as required by 2.1(c) of the Public Lighting Code.

- Currently there is only one LED light product approved for replacement of MV80 lights despite there being more products available. This means that there is an effective monopoly at the supply level and limited price competition for supply which also does not minimise costs for customers.

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- Council would prefer that distribution networks maintained a reasonable list of current standard options and that this was not reliant on the customer requesting the list be updated, although we realise that this would require a change to the public lighting code and is not in control of the AER.

Distribution companies have not got a good track record of communicating proactively and collaboratively.

- Clause 5.2.1 of the public lighting code required distributors to provide a range of regular information to customers. Of the 6 items listed, currently UE has only provided council with reports that cover 2 of these and the report for one of these items covers several customer areas so it is not possible to assess performance for each customer. Citipower has provided even less and does not provide Glen Eira with a service performance report at all, but only an inventory.

Other issues – asset management

Council realises that this is outside the scope of your review and would likely need to be explored at another time or in another process. However it is not an issue that can be easily be solved by any one agency – it would require cooperation and consideration of policy issues by several agencies including the AER. Therefore, we are raising it with the AER as one of those agencies.

- Currently the way street lighting assets are accounted for by distribution companies is not in line with best practice accounting because it does not correlate with the asset base within a Council area. Best practice accounting would write down the book asset over the same time as the life of the physical asset so that if councils are replacing end of life assets, there would be no written down value remaining. The costs associated with lights would all be paid during the lifetime of the asset.

- The problem with the current approach is that when a Council changes end of (physical) life assets, it is often required to pay out a remaining (book) written down value to the distribution company. This relates not to the real remaining asset value, but either to costs incurred in the past or costs incurred in other Council areas.

- The effect of this is that the costs of old lights are artificially low during their lifetime and the impost of this charge at the point in time new lights are installed artificially overstates the costs of installing efficient lights. Both of these effects are perverse price signals that create barriers to installation of the most cost effective assets when considered over their lifetime.

Thank you again for the opportunity to comment on your issues paper.

Yours sincerely

Rachel Ollivier
Group Manager Environmental Strategy and Services

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